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FUNDAMENTAL PLANKS IN A PUBLIC UTILITY PROGRAM

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I have sometimes spoken of the relation between a city and its privately owned public utilities as an irrepressible conflict. The expressions "traction war," "gas fight," "telephone controversy," "electric light dispute," etc., are familiar to everyone. In the picturesque language of the newspaper and the street, public service corporations have long been described as public enemies, and the attitude of belligerency toward them has become chronic in many, if not most, American cities.

While this antagonism often assumes exaggerated, unintelligent and even fantastic forms, and while there is a substantial community of interest along many lines between the public and the utility corporations, we must not blink the fact that there is a permanent and fundamental conflict of motives between them. No amount of regulation and no possible development of good will and the spirit of coöperation can change the fact that private corporations operating municipal utilities do so for profit and for as much profit as they can get, while the consumers and the public strive to get as much service as they can at the least possible cost.

In this conference, which may properly be regarded as a step in the mobilization of the forces representing the public point of view, we must be very careful in our declarations, for the "enemy" is willing to take everything we give him and turn it to his advantage. Every humane principle that we promulgate for the alleviation of the "horrors of war" will be seized upon by him as the basis of an appeal to public opinion against our methods of warfare whenever we try to do anything effective. A public service corporation rarely admits that what is sauce for the goose is also sauce for the gander.

For example, the principle of state regulation by permanent commissions was put forward in this country a few years ago as a statesmanlike method of protecting the people from the exactions

of the public service corporations, while at the same time giving the corporations a fair deal. We now find that all the corporations have been converted to the idea of regulation. They not only welcome it but insist upon having it. They are so enthusiastic over it that they help write the laws and appoint the commissioners.

Other illustrations are the indeterminate franchise, the option to purchase at a fixed price, amortization of capital out of earnings and regulated monopoly. The public service corporations regard the indeterminate franchise as quite impossible as a substitute for existing perpetual franchises, but strongly urge it as a substitute for franchises that come to an end at inconvenient times. The "fixed price" stands like a stone wall against subtraction but yields itself readily to the friendly process of addition. Amortization provides a mask for the gentle art of making the consumers pay for "dead mules." Regulated monopoly is translated into intrenched monopoly.

The discussion of plans of campaign against high rates, poor service, political interference, financial tyranny and all the rest of the evils which we have set out to smite, can only lead to confusion of counsels unless we clearly grasp certain underlying issues involved in the relations between the cities and the public utilities. Without having definite thoughts on these issues, we can not think straight on anything else, and without knowing what any particular speaker's thoughts upon them are, the rest of us can have no measure by which to gauge the importance or fathom the meaning of what he says.

The underlying issues are:

(1) What shall be the recognized character of public utility investments? Shall they be regarded as speculative and held at the risk of the owners, or shall they be regarded as investments in aid of public credit and be given the same security as investments in municipal bonds? If new investments are to be regarded as non-speculative, shall the cities make good all past losses as well as assume all future risks?

(2) What shall be the attitude of the city toward public utilities as money-earning enterprises. Shall the cities seek to get from the utilities a revenue for the relief of general taxation? Or shall the cities subsidize utilities out of taxes? Shall the cities aim to have the utilities, whether under public or under private ownership, furnish their services at cost, or shall public utilities be required

to pay for themselves out of earnings in addition to being self-supporting?

(3) What attitude shall the cities take toward ultimate municipal ownership? Shall they assume that the utilities are to remain permanently as private investments under private operation? Or shall they assume that ultimately all the standard utilities will be publicly owned? If the latter, shall the cities in their franchise grants and their rate contracts merely take an option for purchase at some future time? Or shall they proceed at once to set in motion machinery that will ultimately bring municipal ownership about?

I shall answer categorically, according to my lights, the questions I have propounded under these three heads, and state my reasons for the answers given in each case.

(1) Character of the Investment

Public utility investments should be placed upon a non-speculative basis, and their security should approximate that of municipal bonds.

In the establishment of the non-speculative character of these investments, cities should not undertake to make good past losses, unless they are compelled to do so by franchise contracts.

So far as future investments in the standard utilities are concerned, the cities should assume the risks of loss due to unforeseen causes, and should substantially guarantee the integrity of all investments made at the request or with the approval of public authority.

Public utility investments in the past, with some exceptions, have been highly speculative. There has been a continual buzz of promoters around city councils and state legislatures for the grant of special franchises and charters for public utilities. In most cases the sole purpose of these promoters has been either to sell the franchise or charter outright, or to construct the utility, heavily overcapitalize it and then sell its securities for a much larger sum than the amount actually invested.

Public utilities are not always gold mines. A great deal of money has been lost in premature investments, and a great deal more has gone to the scrap heap with changes in the arts. Experience shows that the public suffers along with the investors when utilities find themselves "hard up." Without money to make adequate exten-

sions and improvements, or even to keep their plants in proper repair, public utilities cannot render the service which is properly demanded of them.

Public utility service, as an essential public function, ought not to be dependent upon a throw of the dice by the manipulators of stocks and bonds. It ought not to furnish an opportunity for any man or set of men to "get rich." It ought to furnish to multitudes of people of comparatively small means a safe and conservative investment for their savings. I am strongly of the conviction that it is disgraceful to a city to have its public service corporations in receivers' hands—almost as disgraceful as it would be for the city to default on its own bonds.

The elimination of the speculator and the stock-jobber from the utility field and the establishment of utility investments upon a safe, conservative, non-speculative basis, is to my mind a fundamental condition precedent to good service, permanently low rates and adequate public control. If capital is made secure and is guaranteed a steady return, it demands nothing more than the ordinary interest rate. Under these circumstances, we should not have to pay premiums to reward capital for a risk undertaken in embarking upon public utility enterprises. There would be no risk. The only special reward offered would naturally go to the men who actually operate the property; for when security and a sure return have overcome the characteristic timidity of money, we have then only to seek a means for enlisting the motive of men for efficiency and economy in the operation of the plant. This cannot be done by lavishing unasked rewards upon capital as such.

Our friends, the public service corporations, will welcome with open arms the proposition that security of the investment is the first and most fundamental plank in any rational program of public utility regulation and development. They are willing to make peace with us on these terms alone. I have said, however, that in my judgment, cities ought not to make good past losses on investments that were frankly on a speculative basis when they were made. I suppose that we are bound to allow for a considerable taint of human nature in the characters of those who own and operate public utilities, even in the "soulless corporations." I suppose that we must frankly concede to them the right to *pursue* the policy of keeping all they have and getting all they can. If we offer them security,

and do not ask for payment, naturally they will take our gift. They have been used to receiving gifts from the cities and are not ashamed to be public beneficiaries. We find them at this moment engaged with their eminent counsel and engineers in attempting to prove to the satisfaction of the court that whenever a public utility has lost money in the operation of its plant, its property is thereby made much more valuable, either in a rate case or in a purchase case. But these same eminent counsel and engineers are employed to prove also that where a utility has made lots of money, it is likewise thereby made much more valuable, either in a rate case or in a purchase case. The companies ask the cities to pay them a premium equally for their losses or their profits. This is the old game of "heads I win, tails you lose." It seems incredible that this double play should be made successfully before the regulating authorities of the country. And yet in many cases it is being done. When the companies have lost, they protest vociferously that they have been mere public agents, spending money for the benefit of the city and its citizens. But when they have won, they forget this agency theory entirely and fall back upon the entrenchments of private property and contractual rights established in the federal constitution. Then they have been doing business strictly on their own account, and the city will interfere at its peril.

I have great admiration for the genius of the writer who composed the famous couplet:

"When the Devil was sick, the Devil a monk would be;
When the Devil was well, the devil a monk was he."

It has many applications, and its application to the attitude of public service corporations toward public control is by no means the least important of them.

Aside from the fact that it is logically preposterous for the cities to make good the speculative losses of the past, such a course would be financially disastrous. It would mean the acceptance and guaranty of the over-capitalization which has brought many utilities into bankruptcy under private management. We may as well dismiss the pretty dream that a city will acquire municipal ownership by giving its bond to Shylock for a pound of flesh, taken nearest the heart, with all the blood that goes with it. When we acquire utilities or recognize their capital value in rate regulation

or franchise contracts at a figure double or treble the value of the physical property, and pay for them in bonds or impose upon the rate payers the perpetual burden of supporting this inflated valuation, we do not secure municipal ownership or public control. Instead, we strengthen and make secure the control already exercised by the owners of public utilities. Mere title is of small importance. The mere fact that rates are fixed by a public service commission, by ordinance or by a contract, has a very limited significance. If we have bound ourselves to pay more than the property is worth and have not paid it, we may be much worse off than if we had not promised. If we fix rates on the basis of an inflated valuation, our position may be much weaker than if we had not fixed rates at all.

If future investments in public utilities are to be non-speculative, someone besides the investors must carry the risk. If we frankly adopt the theory of public agency, which is clearly indicated in the title "public service corporations," there can hardly be any question as to the shoulders upon which the burden of the risk should fall. It is for the service of the public that utilities are established and maintained. More and more, as time goes on, the public nature of these services becomes apparent and imperative. Interruption of service cannot be tolerated. Under the modern organization of society, individuals cannot render utility services for themselves, except at such enormous cost as would make modern city life impossible. Therefore, as seems clear to me, the public should carry the risk of the investment. But, if the cities are to assume the risks of the future in order to give stability to capital, and thereby to secure low rates and dependable service, it is clear that the control of the investment by public authority must be much more minute and far-reaching than it has been in the past.

(2) Public Utilities as Money-Earning Enterprises

In my judgment, public utilities should not be regarded as a legitimate source of profit to be used for the relief of general taxation.

Compensation for franchise grants, and special taxes or license fees imposed upon public service corporations, should not be encouraged, unless the proceeds of such compensation or taxes are to be used in paying for the property.

Every individual public utility should be made to render a clear account of itself and, as a general rule, should be self-supporting.

Public utility services should be rendered as nearly at cost as practicable, except that the rates should include a sufficient contribution to retire the investment within a definite period of time.

Public utilities should receive credit for all the service rendered by them to the city and its various departments, but only under unusual conditions should the city assume to subsidize a public utility service out of the proceeds of taxation or otherwise.

It is not inconceivable that the time may come when public utility services will be furnished free, as elevator service is, but for the present at least, in view of the habits of the people and the financial limitations of the cities, each public utility should continue to be operated on the basis of charging those who use it adequate fees for the service rendered. On the other hand, it seems unfair and unstatesmanlike to attempt to levy a special tax upon the patrons of any particular utility. Possibly the practice of taxing property devoted to the use of public utilities the same as other property held by private individuals may be justified; but except in those cases where taxation is used as a weapon to secure control, it seems that at least the utility property located within street limits should not be taxed. I should be willing to exempt from ordinary as well as special taxation all property actually devoted to public use in the rendering of utility service, under adequate control, but I hesitate to advocate, at the present time, so radical a proposal. I would not, however, advocate the relief of public utility property from the burdens of taxation, and plenty of it, if such relief is to be merely a special privilege to be reflected in increased private profits.

While each of the public utilities should in the main be self-supporting and independent, there is a certain community of public interest among them. Conditions may arise, therefore, under which the rule I have laid down should be modified to the extent of allowing us to take easily earned profits from a strong utility to wipe out the easily incurred deficits of a weak one.

I have said that the rates and charges should include enough to maintain a sinking fund for the retirement of the investment. This requires explanation and defense. It anticipates in a measure our discussion of ultimate municipal ownership. I do not mean that the patrons of a public utility should contribute a sufficient sum to the earnings to enable a public service corporation to pay

off its bonds and still retain full title to the property. I mean that under public ownership, or, under private ownership, as a means of ultimate public ownership, the consumers should be required to pay for the plant and give it to the city. It is often urged that this policy would impose an unreasonable hardship upon a single generation of public utility patrons. It might also be urged that the patrons of a public utility represent a class and therefore should not be required to buy a great property and turn it over without charge to the community as a whole. These objections have certain apparent weight. It seems clear to me, however, that the amortization plan will save a considerable portion of its own cost by making the investment doubly secure and thus reducing the rate of charge for capital under either private or public ownership. Moreover, we have experienced so many disasters and are on the brink of so many more as a result of the reckless financiering of the past, both as to public improvements and as to privately owned public utilities, that we should adopt every possible measure to get these enterprises upon a conservative financial basis. While a number of utilities at the present time seem very well established, all of them have been largely transformed within a generation, and we have no absolute assurance that the investments in any of them will not become obsolete within a single generation. If the public is to assume the risk of obsolescence, it will be a safe and highly reasonable policy to meet obsolescence in advance. Then if the utility continues to be useful, both the consumers as such and the city at large will enjoy a distinct advantage. If, on the other hand, the utility or the property now used by it becomes obsolete, we shall avoid the unhappy condition of still being in debt for property that has disappeared. Where a city is able to enter upon municipal ownership at once and take care of the sinking fund by means of taxes, I have no objection to that course, but I feel that it is a great deal better to require the consumers in one generation to pay for a public utility plant, in addition to maintaining it, than it would be not to have it paid for at all.

Water works and lighting plants are so essential to the city in the performance of its governmental functions that where necessary a city may reasonably contribute out of taxes a very considerable proportion of the income necessary to make such utilities self-sustaining. This contribution is in reality only a payment for services

rendered and should not be regarded as a subsidy. New York City has gone a step further and has put its credit and its taxing power behind a great rapid transit enterprise in order to secure for its citizens a high standard of widely extended service at the five-cent standard rate of fare. Philadelphia is now talking of assuming a similar contingent liability in the case of the local transit lines. I do not wish to be understood as condemning this idea, but I will say emphatically that in my opinion a city ought not to enter upon the policy of subsidizing public utilities until it has absolutely eliminated the speculative element in them so far as the private investment is concerned.

(3) *Ultimate Municipal Ownership*

In my opinion, cities should *not* assume that public utilities are to remain permanently as private investments under private operation.

On the contrary, they should assume that all the well-established utilities will sooner or later be publicly owned, private capital being entirely excluded from the public streets except as it is loaned to the city.

In their franchise grants, and in all contracts affecting rates or granting privileges, the cities should establish the option to take over the utilities either at pleasure or at reasonable fixed intervals.

Wherever possible, the cities should go still further and without more delay definitely set in motion the machinery necessary to compel the gradual withdrawal of private capital from the public streets and the gradual acquisition of the utility plants by the cities as public property.

This brings us squarely to a consideration of the theory of municipal ownership. I call specific attention to the fact that municipal ownership of the fixtures in the streets presents no serious obstacle to the operation of public utilities by larger units. It is apparent that the development of interurban utilities, the extension of utility service to rural regions and the grouping of a number of cities in relation to a single source of supply often present serious obstacles in the way of separate operation by or for each distinct political unit. I shall assume that the most appropriate governmental agencies for the operation of these utilities will be developed as the need arises, and therefore my argument will be confined to

the desirability of municipal ownership, with or without public operation.

While it is true that in its relation to public utilities, the ultimate demand of the public is the best possible service at the lowest practicable cost, I do not admit that the entire case is to be determined by a comparison of the rates and efficiency of operation of individual public and individual private plants. I have no disposition to deny that serious administrative and political difficulties now obstruct the movement for municipal operation. I take my stand for the immediate adoption of the policy of ultimate municipal ownership on broader grounds. I need not repeat what I have already said in regard to the recognized public character of these services. I need not go at length into the difficulty of adequately regulating a private monopoly. I need not claim greatly reduced rates or greatly improved service as the immediate result of municipal ownership. All these considerations are factors in the great development of city civilization which makes ultimate municipal ownership of public utilities appear to be inevitable, whether we want it or not. But back of all the usual arguments, pro and con, on this subject lies the fundamental fact that the existence of a great body of private capital invested in the public streets is a continuing menace to a city's welfare.

The concentration of the control of enormous masses of the common wealth in the hands of a few men, irresponsible to the community for the manner in which they exercise such control, is in itself a recognized menace to civilization. This applies to all kinds of enterprises, but when we come to public utility enterprises, which are actually performing a public function, and which are constantly in contact with the regularly established political authorities, and which operate by means of easements in public property, the dangers of concentration of control are multiplied.

It is well known that in the great cities the development of land values is such as to make it impracticable for the majority of men to be landholders. Cities create a proletariat, a fourth estate, which, in proportion as it becomes landless, homeless and propertyless, becomes a dangerous element in a democracy. Political and economic stability rest upon widespread participation in wealth. The conditions that prevail in modern cities in certain respects tend to cultivate the most dangerous factors in democracy. Cities by their

very nature are coöperative, and public utilities, *par excellence*, are the visible symbols of that coöperation. If in the cities we are passing out of the stage of widespread individual ownership, our only safe course is to develop a strong community ownership, not a mere sentimental loyalty attaching to the city that we love, but a substantial universal economic interest in it. Capital is too valuable to society to be wastefully destroyed. We all respect it. If we destroy it, we are destroying that which ultimately belongs to the community. The public ownership of public utilities, which is merely the complete public ownership of the public streets, not only frees the agents of the people from the compelling influence of invested private capital, but gives those agents and the people they represent a new sense of responsibility, a new sense of civic loyalty and a new attitude of conservatism, all of which are of the utmost importance in the orderly development of our civilization.

This matter of municipal ownership is a long story. I can hardly hope, in the time available this morning, to convince anyone whose mind is already set the other way. I maintain that municipal ownership, as an ultimate policy, is both desirable and inevitable, but the real point of my argument here is that, if it is either desirable or inevitable, the cities should begin to prepare for it now. I sometimes think that the warm opponents of municipal ownership and operation, in their zeal to show that our cities are politically unfit to undertake public utility enterprises, tend to gloat over the proofs they find, as if they were really glad that the cities in which they live are incapable or unfit to undertake these functions of such grave concern to everyone. It seems to me that at least all of us who take the public point of view, are bound to strive to make our cities fit for municipal ownership and operation, if they are not so already. *We* at least can have no sympathy with the attempts being made on every hand to hinder, hamper and render abortive the municipal ownership movement. *We* at least can not approve of the attitude of those who are willing to saddle the city with an enormous overcapitalization as its initial handicap when it undertakes municipal ownership. *We* at least can have no sympathy with the efforts constantly being made to pack commissions and councils with weak or private minded men who will effectively prevent or postpone the development of efficient and intelligent public agencies able, in case of need, to make municipal ownership a success.

The problem that the cities must ultimately meet, and that they should begin to meet definitely now, is the problem of paying for the public utilities so that the actual transfer of the property from private ownership to public ownership may be ultimately made. It is a mistake to assume that a reduction of rates will bring public ownership any nearer, except as it may squeeze the illegitimate values out of franchises and render the public utility field uncongenial for speculators. Whenever a city has an opportunity, in the granting of a new franchise or in the making of a contract, to secure an option for the purchase of a public utility at a reasonable fixed price, it should do so, but in such cases it should place the exercise of that option and the provision for the payment for the utility ahead of rate reduction in its program. If we secure an option to buy a utility at a fixed price and then reduce the rates to a point where nothing can be saved from earnings for an amortization or purchase fund, we make the future acquisition of the property more rather than less difficult. For unless we are willing to pay for the utility out of taxes, it will be very unpopular and very difficult, having pared the rates to the bone, to increase them again for the purpose of establishing a sinking fund.

You may not all agree with me in my attitude on the three fundamental issues which I have propounded here today, but I maintain that what you say or what I say about general public utility problems can be of very little importance to ourselves or to anybody else unless we know what we think on these issues and make our thoughts known. I repeat the three questions:—

1. Should public utility investments be speculative or non-speculative?
2. Should public utilities be exploited for the benefit of the taxpayers or should they be operated on the theory of rendering service at cost?
3. Should the cities, *now*, take all possible steps to prepare the way for ultimate municipal ownership?